

## Message Text

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TO SECSTATE WASHDC 5386

INFO AMCONSUL BOMBAY

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UNCLAS NEW DELHI 5722

E.O. 11652: N/A

TAGS: EING, IN

SUBJECT: FOREIGN EXCHANGE REGULATION ACT (FERA) GUIDELINES  
AMENDED

1. SUMMARY: THE FERA GUIDELINES HAVE BEEN AMENDED TO ALLOW  
FOREIGN FIRMS TO RETAIN 51 PERCENT EQUITY IN A JOINT VENTURE IF  
PRODUCTION OF SOPHISTICATED TECHNOLOGY PRODUCTS AND/OR EXPORTS ACCOUNT

FOR 60 PERCENT OR MORE OF THE FIRMS TOTAL PRODUCTION. SUCH COMPANIES  
WILL BE REQUIRED TO UNDERTAKE A 10 PERCENT EXPORT COMMITMENT.  
FOREIGN COMPANIES WILL CONTINUE TO BE ALLOWED 74 PERCENT EQUITY IF  
75 PERCENT OF PRODUCTION IS SOPHISTICATED TECHNOLOGY PRODUCTS OR  
EXPORTS. IF A COMPANY EXPORTS 100 PERCENT OF ITS PRODUCTION  
THE FOREIGN PARTNER MAY BE PERMITTED TO HOLD 100 PERCENT  
OF THE EQUITY. IF NONE OF THESE CONDITIONS ARE MET, THE FOREIGN  
FIRM MUST REDUCE ITS EQUITY TO 40 PERCENT. END SUMMARY.

2. DEPUTY FINANCE MINISTER SUSHILA ROHTAGI IN A STATEMENT TO  
PARLIAMENT ON APRIL 15 OUTLINED A MAJOR CHANGE IN FERA  
GUIDELINES OF DECEMBER 20, 1973. THE CHANGES APPLY TO BRANCHES  
OF FOREIGN COMPANIES OPERATING IN INDIA AND INDIAN SUBSIDIARIES  
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IN WHICH THE NON-RESIDENT EQUITY INTEREST IS IN EXCESS OF 40

PERCENT. THE FERA GUIDELINE HAVE BEEN AMENDED TO ALLEVIATE DIFFICULTIES IN INTERPRETING AND IMPLEMENTING THE EXISTING REGULATIONS.

3. THE FOLLOWING ARE THE PRINCIPAL AMENDMENTS/CLARIFICATIONS MADE TO THE 1973 GUIDELINES BY THE NEWLY ISSUED STATEMENT:

A. IF THE COMBINED ACTIVITIES OF A COMPANY ENGAGED IN CORE SECTOR PRODUCTION AND EXPORTS ACCOUNTS FOR NO LESS THAN 75 PERCENT OF THE TOTAL ANNUAL TURNOVER THEN SUCH COMPANIES WILL BE ALLOWED TO CONTINUE TO OPERATE WITH A NON-RESIDENT EQUITY HOLDING OF 74 PERCENT;

B. COMPANIAS WHOSE COMBINED CORE SECTOR PRODUCTION, USE OF SOPHISTICATED TECHNOLOGY, AND EXPORTS TOGETHER ACCOUNT FOR NO LESS THAN 60 PERCENT OF THEIR ANNUAL TURNOVER, WILL HENCEFORTH BE PERMITTED TO OPERATE WITH 51 PERCENT FOREIGN EQUITY HOLDING. ALL SUCH COMPANIES WILL BE REQUIRED TO UNDERTAKE TO BEGIN TO EXPORT A MINIMUM OF 10 PERCENT OF THEIR TOTAL ANNUAL TURNOVER WITHIN A PERIOD OF NOT MORE THAN TWO YEARS FROM THE DATE OF APPROVAL BY THE RESERVE BANK OF INDIA TO CONTINUE AT THE 51 PERCENT LEVEL.

C. COMPANIES WITH EXPORTS EXCEEDING 40 PERCENT OF THEIR TURNOVER, IRRESPECTIVE OF CORE SECTOR PRODUCTION OR SOPHISTICATION OF TECHNOLOGY, WILL BE ALLOWED TO OPERATE WITH 51 PERCENT NON-RESIDENT EQUITY. COMPANIES WHICH ARE ABLE TO GUARANTEE HIGHER EXPORT PERFORMANCE ON A SUSTAINED BASIS WOULD BE ELIGIBLE, DEPENDING ON THE MERITS OF EACH CASE, TO CONTINUE AT A HIGHER NON-RESIDENT EQUITY LEVEL.

4. THE 1973 GUIDELINES STIPULATED THAT FOREIGN COMPANIES COULD CONTINUE TO OPERATE WITH 74 PERCENT FOREIGN OWNERSHIP IF THEY WERE ENGAGED IN CORE SECTOR PRODUCTION (INDUSTRIES SPECIFIED IN APPENDIX 1 OF THE INDUSTRIAL LICENSING POLICY OF FEBRUARY 1973): OR WERE PREDOMINANTLY ENGAGED IN EXPORTS (MINIMUM EXPORTS BEING 60 PERCENT OF TOTAL PRODUCTION TURNOVER); OR WERE ENGAGED IN MANUFACTURING OR OTHER ACTIVITIES REQUIRING SOPHISTICATED TECHNOLOGY OR SPECIALIZED SKILLS. COMPANIES FAILING TO MEET ANY OF THESE CRITERIA WOULD BE REQUIRED TO BRING DOWN FOREIGN EQUITY SHAREHOLDING TO A LEVEL OF NO MORE THAN 40 PERCENT. THE CONSIDERATION IN DETERMINING FOREIGN EQUITY ALLOWABLE TO COMPANIES ENGAGED IN MORE THAN ONE BUSINESS ACTIVITY WAS DEPENDENT UPON THE PROPORTION OF CORE SECTOR TO NON-CORE SECTOR ACTIVITY. IF NON-CORE SECTOR PRODUCTION CONSTITUTED ONLY A MINOR

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PART OF THE TOTAL BUSINESS ACTIVITY OF THE COMPANY (NOT EXCEEDING 25 PERCENT OF THE EX-FACTORY VALUE OF TOTAL ANNUAL PRODUCTION OF RS 50 MILLION WHICHEVER WAS LESS) THEN THE COMPANY COULD CONTINUE TO OPERATE WITH 74 PERCENT FOREIGN EQUITY HOLDING. THE RATIONALE UNDERLYING THE DECISION TO ALLOW COMPANIES MORE THAN 40 PERCENT NON-RESIDENT EQUITY HOLDING, UNDER THE 1973 GUIDELINES, WAS THAT THE PREDOMINANT CORE SECTOR OR EXPORT ACTIVITY CONTRIBUTED SIGNIFICANTLY AND DIRECTLY TO NATIONAL

ECONOMIC AND INDUSTRIAL DEVELOPMENT.

5. THESE AMENDMENTS WILL NOT BE APPLICABLE TO FOREIGN DRUG AND PHARMACEUTICAL COMPANIES.

6. COPIES OF THE GOI STATEMENT HAVE BEEN AIRPOUCHED FOR THE ATTENTION OF STATE (MORLEY) AND USDOC (ADERHOLD).

7. COMMENTS: THE LONG-EXPECTED AMENDMENTS TO THE 1973 FERA GUIDELINES MARKS A MAJOR POLICY DECISION TAKEN BY THE GOI FOR ADMINISTERING SECTION 29 OF THE FOREIGN EXCHANGE REGULATION ACT. THE CREATION OF AN INTERMEDIATE POINT OF 51 PERCENT FOREIGN EQUITY HOLDING AND THE EVALUATION OF INDIVIDUAL COMPANY CASES ON A COMPOSITE BASIS TAKING INTO CONSIDERATION CORE SECTOR PRODUCTION, SOPHISTICATION OF TECHNOLOGY UTILIZED, AND EXPORT PERFORMANCE IS EXPECTED TO REDUCE THE UNDULY ONEROUS CONDITIONS IMPOSED BY THE 1973 GUIDELINES WHICH DID NOT PROVIDE FOR THE COMBINING OF THESE FACTORS. THE AMENDMENTS ARE ALSO INDICATIVE OF THE GOI'S DESIRE TO SOFTEN THE CONDITIONS FOR DILUTION OF EQUITY FROM THE EARLIER GUIDELINES. THE AMENDMENTS WILL APPLY RETROACTIVELY WITH COMPANIES WHICH HAVE ALREADY DILUTED THEIR FOREIGN EQUITY ENTITLED TO AVAIL THEMSELVES OF THE NEW AMENDMENTS. AS A RESULT OF THE AMENDMENTS, THE GOI HOPEFULLY WILL BE ABLE TO MAKE EXPEDITIOUS DECISIONS ON THE 245 OF 855 CASES REMAINING UNDER THE FERA. THE EARLIER GUIDELINES HAD CREATED PROBLEMS FOR THE GOI IN DEALING WITH THE CASES OF MULTI-PRODUCT COMPANIES SUCH AS UNION CARBIDE, PHILLIPS OF THE NETHERLANDS, IMPERIAL CHEMICAL INDUSTRIES AND OTHER WHOSE CONTRIBUTION TO INDIAN INDUSTRIAL DEVELOPMENT AND EXPORTS WAS VITAL BUT WHO COULD NOT MATCH THE STRICT CRITERIA UNDER THE OLD GUIDELINES AND, AT THE SAME TIME, WERE UNWILLING TO COME DOWN TO A 40 PERCENT FOREIGN EQUITY POSITION. FOREIGN CAPITAL IS NOW ASSURED OF A REASONABLE CHANCE TO RETAIN MAJORITY HOLDING AND MANAGEMENT CONTROL FOR INVESTMENT IN INDIA UNDER CONDITIONS WHICH, MOST FOREIGN BUSINESSMEN FEEL, ARE NOT UNDULY RESTRICTIVE.SAXBE

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